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1           Are you suggesting to the Commission that we  
2 would have to have another start up revenue type  
3 requirement that we had at the beginning of NRF?

4           A   This statement is made in the context of a  
5 discussion of the content of purchase price caps. And  
6 the short answer to your question is, yes, I am if in  
7 fact the Commission were to pursue a pure price caps  
8 approach.

9           As I explain in the testimony, the current  
10 rate level because of the manner in which it was  
11 developed and the manner in which it has been adjusted  
12 under the NRF since 19 -- since the beginning of 1990  
13 captures embedded cost levels which are simply  
14 inapplicable in a pure price cap regime in which we are  
15 presumably trying to truly simulate the competitive  
16 outcome where we're -- there is no longer any sharing  
17 and the company is in effect permitted to behave in the  
18 marketplace, assume risks in the marketplace and  
19 generate rewards in the marketplace that are essentially  
20 identical to that which would be reasonable to a  
21 competitive firm.

22           So my testimony is that if the Commission were  
23 to adopt pure price caps and to eliminate sharing, then  
24 a reinitialization of rate levels to their TSLRIC-based  
25 levels to exclude any excessive embedded or unrecovered  
26 embedded cost levels is both necessary and appropriate.

27           Q   Okay. On page 26 of your testimony  
28 Dr. Selwyn, at line 6, you refer to an offset against

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1 non-book asset gains.

2 And just for my own edification, what are  
3 non-book asset gains that you're referring to here?

4 A I've discussed that extensively in my  
5 testimony. And a non-book asset is a property that is  
6 of value to a corporation that is capable of generating  
7 revenue and income for the corporation but which for  
8 reasons of accounting convention, does not appear as a  
9 capital as set on the companies books.

10 For example, the appreciation in value of an  
11 intangible asset such as brand identification or  
12 customer lists or the capability of exploiting an  
13 embedded infrastructure to generate additional revenues  
14 that in non-regulated competitive services that up to  
15 now may not have existed all constitute an appreciation  
16 value of non book assets.

17 We saw this kind of thing occurring, for  
18 example, in the case of the cellular industry where the  
19 licenses were acquired at -- by the wireline carriers at  
20 zero cost and yet have over the years escalated in  
21 market value to quite substantial levels.

22 Q When you said they don't appear on company  
23 books, you mean there is no USOA account that they're  
24 booked to; isn't that correct?

25 A That's correct. And similarly, there's no  
26 financial -- generally speaking, those assets are not  
27 reflected on the company's GAAP-type books either,  
28 GAAP.

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1           Q   Dr. Selwyn, do services with higher demand  
2 growth generate higher productivity gains for a company  
3 than prior growth services operate -- generate?

4           A   All other things being equal, are we speaking  
5 of LECs specifically or did you want me answer that  
6 question for the world at large?

7           Q   The world at large.

8           A   Is that right?

9               Well, the principle here has to do with the  
10 nature of the production function.

11           If there are economies of scale present in the  
12 production function, then we would tend to expect, all  
13 other things being equal, services with higher demand  
14 growth to exhibit proportionately higher productivity  
15 gains than services with lower demand growth.

16           But we would also expect that to -- an  
17 influence in factor that would be the extent to which  
18 the service -- the production function for the service  
19 is labor versus capital intensive.

20           So for example, switched access and long  
21 distance services would tend to exhibit higher  
22 productivity gains if they were -- if they could be --  
23 their costs and input -- inputs and outputs could be  
24 isolated than for the aggregate of all LEC services.

25           Q   Thank you, Dr. Selwyn.

26           Now on page -- I'd like you to turn to your  
27 reply testimony, Exhibit 63, and I'd like you to take a  
28 look at line 11, 12?

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1 A Of what?

2 Q Of page 13. Thank you very much.

3 I'm trying to talk slower so it takes me  
4 awhile to get to the page numbers.

5 (Laughter)

6 MR. GOLABEK: Q At page 11, and I guess you had  
7 made it in your direct -- at page 13 on line 11, I guess  
8 you had made a similar statement.

9 In your direct testimony, you state that  
10 effective competition is not likely to rapidly develop  
11 in the foreseeable future.

12 Now isn't it true, Dr. Selwyn, that you didn't  
13 personally conduct any studies which analyze or forecast  
14 how quickly competition will develop in California?

15 A The statement -- no, I did not conduct such  
16 studies. The statement is not based upon -- I don't  
17 think such a study could be conducted. It was just a  
18 simple answer.

19 Q It's also correct that you're not privy to any  
20 plans AT&T or MCI might have internally for entry into  
21 the local exchange market, are you?

22 A I have some knowledge of AT&T's plans in the  
23 local exchange market.

24 Q And what knowledge do you have?

25 MR. FABER: Your Honor, I'm going to have to stop  
26 now and object to the possibility that that might be  
27 proprietary information.

28 I don't know -- Dr. Selwyn will probably tell

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1 us -- but I would like to be careful to protect any  
2 interests that AT&T might have in the answer to this  
3 question.

4 MR. STOVER: I appreciate that, your Honor, and I  
5 have confidence in Dr. Selwyn that he will not reveal  
6 proprietary information, so I'm not objecting to that  
7 question.

8 MR. FABER: So do I have confidence that Dr. Selwyn  
9 won't reveal any proprietary information. I just wanted  
10 to make clear that the record was clear from the --

11 MR. STOVER: And I thank Mr. Faber for his  
12 solicitude.

13 ALJ REED: Dr. Selwyn.

14 THE WITNESS: AT&T has indicated plans in initially  
15 entering the local exchange market as a  
16 nonfacilities-based reseller of LECs services. It has  
17 announced these plans in several states.

18 And my firm has done some analytical work and  
19 prepared testimony for AT&T on that subject. That's the  
20 source of my knowledge.

21 MR. GOLABEK: Q And California's one of those  
22 states?

23 A Yes.

24 Q And this -- I didn't hear you. Did you  
25 respond?

26 A It is, yes.

27 Q Thank you.

28 And those plans call for entering into the

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1 local market in 1996; is that correct?

2 MR. STOVER: I would object to that market -- the  
3 timing of AT&T's market entry is proprietary  
4 information, and I would object on that basis.

5 MS. BURDICK: I would also object as vague and  
6 ambiguous. Dr. Selwyn testified that AT&T's plans in a  
7 number of states and the question did not refer to a  
8 particular statement wherein those plans may differ from  
9 state to state.

10 MR. GOLABEK: Well, it was follow-up to the  
11 question to California, but I will withdraw the  
12 question, your Honor.

13 ALJ REED: Thank you, Mr. Golabek.

14 MR. GOLABEK: Q Now, you've made forecasts to the  
15 Commission in the past about how future events will play  
16 out in the California telecommunications market; is that  
17 correct, Dr. Selwyn?

18 A Yes.

19 Q Now isn't it true that your last estimate to  
20 the Commission, your last forecasts for the Commission  
21 of a negative .723 elasticity for the interLATA toll  
22 market was not accurate?

23 MR. FABER: Objection, your Honor. We had -- I  
24 attempted to cross-examine some of the witnesses for the  
25 LECs on elasticity and I -- all those questions were  
26 objected to by Pacific Bell and by GTEC. And for  
27 Mr. Golabek to now start asking questions about  
28 elasticity seems highly inappropriate.

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1       MR. GOLABEK: Your Honor, he's asking this  
2 Commission to accept his expert opinion on what will  
3 happen in the future.

4       Throughout his report he makes projections  
5 about whether or not competition will or will not  
6 rapidly develop in the foreseeable future among other  
7 things, and I'm just trying to examine his track record  
8 and ask him if that was his forecast -- and point out  
9 that he's been inaccurate in the past.

10       MR. FABER: If that's what he's trying to do, I  
11 wasn't clear that that's what he was trying to do, I  
12 will object further for a lack of foundation.

13       The question was, isn't it true that the  
14 negative .723 estimate was wrong? And I'd like  
15 Mr. Golabek to produce for the record the evidence of  
16 what the elasticity has been to date specifically so  
17 that we can examine that question rather than requesting  
18 Dr. Selwyn who doesn't have the details of the LEC's  
19 toll revenues to tell.

20       MR. GOLABEK: Sorry, Mr. Faber. I didn't mean to  
21 interrupt.

22       His projection is recorded in IRD, so I'll  
23 withdraw the question also.

24       ALJ REED: Thank you, Mr. Golabek.

25       MR. GOLABEK: Q Now, Dr. Selwyn, I'd just like to  
26 confirm a few things here and few minor points.

27       It's true you have a degree, Bachelor's degree  
28 in Economics; is that correct?

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1           A    That's correct.

2           Q    And you have a Master's degree, a Master's of  
3 Science degree in Industrial Management?

4           A    That's correct.

5           Q    And your Ph.D. is in Management?

6           A    That's correct.

7           Q    Dr. Selwyn, you've stated that you've been  
8 retained by the CCLTC for purposes of this proceeding.  
9 Can you tell us what the hourly rate you are charging  
10 CCLTC is?

11          A    My hourly rate is \$250 an hour.

12          Q    Okay. And how long did it take you to prepare  
13 your testimony that you put into this proceeding?

14          A    I'm trying to recall.

15          Q    An estimate, if you can.

16          A    Well, several members of my staff worked on it  
17 in addition to myself. But I would estimate that  
18 between the direct and the rebuttal, there were probably  
19 in the range of 150 to 200 hours total, not all of which  
20 was mine.

21          Q    Sorry. I didn't mean to cut you off there.

22               And you attended this hearing on prior  
23 occasions in this particular proceeding; isn't that  
24 correct?

25          A    I was here last week, yes.

26          MR. GOLABEK: That's all I have for Dr. Selwyn,  
27 your Honor.

28          ALJ REED: Thank you, Mr. Golabek.



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1 EXAMINATION

2 BY ALJ REED:

3 Q Dr. Selwyn, I have one question for you. ]

4 Would you recommend lowering your proposed  
5 productivity factor if effective competition were  
6 demonstrated?

7 A The productivity factor that I am recommending  
8 is based upon what I believe is still a conservative  
9 estimate of the potential productivity gain. If  
10 effective competition were shown to exist broadly across  
11 all segments of the LECs market, then the need for  
12 continued economic regulation would evaporate.

13 My concern is that if there is effective  
14 competition in some segments and there remains  
15 substantial monopoly in others, that the opportunities  
16 for cross-subsidization of the competitive services by  
17 those remaining monopoly services is in no sense  
18 diminished relative to that which might exist even today  
19 with very limited competition.

20 And in that sense the need to have a  
21 continuation of a price protection for the services that  
22 remain monopolistic is undiminished. So as a general  
23 matter I would not support a proposal that would tie the  
24 X factor to the development of partial competition.

25 I think that if we actually were to have  
26 extensive full competition segments, then economic  
27 regulation itself could then be eliminated.

28 ALJ REED: Thank you, Dr. Selwyn.

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1           Mr. Faber, before I get to whether or not you  
2 have redirect, what we are going to do with this Salomon  
3 Brothers' report is, Mr. Sasser, you want this document,  
4 this exhibit to go into the record; is that correct?

5           MR. SASSER: Yes, your Honor.

6           ALJ REED: What I would like is for you to submit  
7 the entire document. It may not be today. It may be  
8 that you will submit that as a late filed. But I will  
9 reserve the number Exhibit No. 65.

10                   (Exhibit No. 65 was marked for  
11                   identification.)

12           ALJ REED: You withdrew the question that you had  
13 on this page. So the full document will be in the  
14 record. And that gives parties the freedom to, within  
15 their briefs, expand on any context concerns that they  
16 have.

17           Mr. Faber, did you have any redirect?

18           MR. FABER: I would like to request a few moments  
19 off the record to confer with the witness.

20           ALJ REED: Okay. Why don't I give you ten  
21 minutes.

22           MR. FABER: That would be fine, your Honor.

23           ALJ REED: We will be back at 10:15.

24                   (Recess taken)

25           ALJ REED: On the record.

26           Mr. Faber.

27           MR. FABER: Yes, your Honor, I have some brief  
28 direct for Dr. Selwyn.

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1 ALJ REED: Redirect.

2 MR. FABER: What did I say?

3 ALJ REED: Direct.

4 REDIRECT EXAMINATION

5 BY MR. FABER:

6 Q Dr. Selwyn, you were asked whether services  
7 with a higher demand growth exhibit a higher  
8 productivity than services with lower demand growth, do  
9 you recall that?

10 A Yes.

11 Q Can your answer be taken as implying a  
12 long-term relationship between productivity and demand  
13 growth, or was it limited to comparing services with  
14 high growth versus low growth in the current time frame?

15 A It was definitely the latter. I interpreted  
16 the question as implying that as well. In the long run,  
17 companies can make adjustments in their cost structure  
18 to compensate for sustained changes in the level of  
19 demand. So that, for example, if there is a fundamental  
20 change in demand growth due to, for example, the entry  
21 of competition, then that can be captured in changes in  
22 capital investment and other costs.

23 As I noted in my testimony, LECs are currently  
24 replacing something between 10 and 11 percent or so of  
25 their installed plant base each year so that there is  
26 ample room for cost adjustment to accommodate sustained  
27 demand changes.

28 I was referring in that answer simply to

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1 different growth rates among current services such as  
2 switched access and interstate services which tend to be  
3 high growth versus local exchange dial tone lines which  
4 tend to be relatively low growth service which is more  
5 tied to population growth than to any other factor.

6 Q Dr. Selwyn, you were also asked about some  
7 statements made on page 13 of your reply testimony at  
8 lines 10 and 11 regarding the likelihood of the rapid  
9 development of effective competition. Do you recall  
10 that?

11 A Yes.

12 Q And you were also asked some questions about  
13 AT&T's entry into the local exchange market in  
14 California. Do you recall that?

15 A Yes.

16 Q And you said that AT&T's initial entry  
17 strategy is to be a nonfacilities-based reseller of  
18 local exchange services?

19 A That is my understanding, yes.

20 Q Are you aware of the fact that yesterday  
21 Pacific Bell announced publicly that it intends to  
22 provide resale of its local exchange services at its  
23 cost?

24 MR. SASSER: Objection, your Honor. I think that is  
25 beyond the scope of direct.

26 MR. GOLABEK: I would join in the objection.

27 MR. FABER: I would be happy to explain.

28 Mr. Golabek asked Dr. Selwyn about whether he thought

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1     there was going to be effective competition rapidly  
2     developing.

3           MR. GOLABEK: No, I did not. That is a  
4     mischaracterization. I asked if he had any studies --  
5     whether he personally conducted any studies which  
6     analyzed how quickly competition would develop in  
7     California.

8           MR. FABER: I think there were several questions  
9     asked about this, your Honor. But the fact is that he  
10    asked him about a sentence that appears on page 10 and  
11    11 -- lines 10, 11 and 12 of page 13 of the reply  
12    testimony.

13           All I am intending here to show is that in  
14    fact Dr. Selwyn does have support for that statement. I  
15    think that Mr. Golabek is wrong in objecting because he  
16    asked about support and that is all I am after now.

17           MR. SASSER: Your Honor, asking about Pacific  
18    Bell's filing I don't think has anything to do with  
19    support for Dr. Selwyn's knowledge of AT&T's plan.

20           MR. FABER: Again, they are misunderstanding, your  
21    Honor. The question is that Dr. Selwyn already said  
22    that AT&T intends to be a nonfacilities-based reseller  
23    as an entry strategy. My question goes to whether or  
24    not AT&T or any other reseller will be able to  
25    effectively compete with Pacific Bell given a public  
26    announcement that Pacific Bell is going to charge \$24  
27    for resale of a service that it sells for \$11.25.

28           MR. SASSER: Your Honor, that is an outrageous

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1 attempt to introduce evidence that is not in the  
2 record. We are now going to get into litigation of  
3 Pacific Bell's costs and provision of resale services.  
4 It is far beyond the scope of the cross.

5 MR. STOVER: May I be heard briefly on this?  
6 Simply that the eagerness of these two attorneys to  
7 object to this question is directly related to the  
8 inadvisability of the line of questioning that they  
9 opened up. And, your Honor, they have to live with the  
10 consequences of the areas that they have opened up.

11 Dr. Selwyn has testified that the evolution of  
12 effective competition is likely to be slow, and they  
13 asked him for the basis for that. And now Mr. Faber is  
14 going to probe further on the question of the basis for  
15 his assertion. It is entirely appropriate. And I  
16 understand their eagerness to avoid it, but they opened  
17 the door and Mr. Faber is merely walking through.

18 MR. GOLABEK: Your Honor, may I respond. There is  
19 no eagerness to avoid the question necessarily. The  
20 scope of redirect is to follow up on questions that I  
21 have asked and the limited areas I got into.

22 I asked three areas, whether he has personally  
23 conducted studies, privy to AT&T plans, and he said he  
24 was, and what was AT&T's plans. That was it. That was  
25 all. What they are trying to do is supplement the  
26 record.

27 I think Mr. Faber said to begin with he wants  
28 to offer some direct testimony. I know it was a slip of

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1 the tongue, but that is exactly what they are attempting  
2 to do at this particular point.

3 MR. FABER: That I object to because I said  
4 redirect. Your Honor misheard me and Mr. Golabek  
5 misheard me. I said redirect. I did not say direct. I  
6 resent the insinuation Mr. Golabek is making by that  
7 statement.

8 MR. GOLABEK: Nonetheless, I think this is beyond  
9 the scope, and this would be in the nature of direct and  
10 additional testimony, your Honor.

11 ALJ REED: Mr. Golabek, when you started your  
12 questioning of Dr. Selwyn, you asked him -- he let you  
13 know that he had some information about AT&T, but your  
14 question was broader than that. You asked about larger  
15 concerns.

16 Now, Mr. Faber, that you know what  
17 Mr. Sasser's concern is in your question, can you ask  
18 the questions that you intend in clarifying this area,  
19 can you rephrase the question?

20 MR. FABER: I can try, your Honor.

21 Q Dr. Selwyn, you are aware of the current local  
22 exchange rates that Pacific Bell and GTEC charge in this  
23 state?

24 A Yes.

25 Q Do you believe that it would be possible for  
26 effective resale competition to develop in this state if  
27 either or both of them offered their local exchange  
28 services for resale at a rate exceeding \$20?

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1       A    It would be extraordinarily difficult unless  
2   the facilities-based resellers were prepared to accept  
3   continuing losses. And it is difficult for me to  
4   understand why they would be willing to do that.

5       Q    Finally, Dr. Selwyn, would you turn to  
6   Exhibit 64, the single-page excerpt that Mr. Sasser has  
7   introduced from the Salomon report.

8       A    Yes.

9       Q    Mr. Sasser asked if you agreed that a  
10   particular sentence appears in full in that report,  
11   beginning with the word "consequently" in the middle of  
12   the page. Do you see that?

13      A    Yes.

14      Q    Do you see that that sentence includes the  
15   phrase "if one accepts the premise that there will be a  
16   free-for-all of sorts with lots of players attempting to  
17   provide branded end-to-end solutions?"

18      A    I see that.

19      Q    Is there any indication that the marketplace  
20   accepts that premise?

21      A    No. In fact, the thrust of my testimony is  
22   that the marketplace does not accept that premise. It  
23   is not even clear that Salomon accepts it because if  
24   they did it is not clear why they would have written the  
25   sentence with that qualification.

26      MR. FABER: That's all the questions I have, your  
27   Honor. Thank you.

28      ALJ REED: Thank you, Mr. Faber.



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1 Dr. Selwyn, you are excused. Thank you very  
2 much.

3 THE WITNESS: Thank you, your Honor.

4 MR. FABER: Your Honor, I would renew my motion for  
5 the admission of Exhibit 62 and 63.

6 ALJ REED: Are there any objections?

7 (No response)

8 ALJ REED: Exhibits 62 and 63 are received into  
9 evidence.

10 (Exhibit Nos. 62 and 63 were  
11 received into evidence.)

12 MR. SASSER: Your Honor, I would move the admission  
13 of Exhibit 64.

14 MR. STOVER: Objection, your Honor. I would object  
15 to the admission of 64. We have provided for the  
16 admission of the entire document in 65. I don't see any  
17 particular reason for the admission of 64. It is  
18 incomplete.

19 MR. SASSER: Your Honor, questions have been asked  
20 about this specific page, and I think for clarity of the  
21 record there ought to be a separate exhibit attached to  
22 it.

23 ALJ REED: Yes, that's fine.

24 Noting your objection, Mr. Stover, Exhibit  
25 No. 64 is received into evidence.

26 (Exhibit No. 64 was received into  
27 evidence.)

28 MS. GRAU: Your Honor, a housekeeping detail. The

Enrollment

**PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA**

Investigation in the Commission's own  
Motion into the Second Triennial Review of  
the operations and safeguards of the  
Incentive-Based Regulatory Framework for  
local exchange carriers

195.15-025

Direct Testimony

of

**LEE L. SELWYN**

on behalf of the

**California Committee of Large Telecommunications Consumers (CCLTC)**

September 8, 1995

Before the  
**PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA**

Investigation on the Commission's own  
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**I.95-05-047**

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## MODIFYING THE NRF TO REFLECT PRODUCTIVITY GROWTH AND INPUT PRICE TRENDS

34

The X factor formula must include the post-divestiture LEC productivity growth *plus* a LEC input price differential *plus* an appropriate "stretch factor," in order to mirror the efficiency incentives found in competitive markets and to ensure ratepayer protections.

34

This Commission should adopt the use of an input price differential based upon post-divestiture experience in setting the X factor, as the FCC did in its 1994 price caps review.

35

Recent "updates" and "corrections" to the original Christensen study do not remedy any of its deficiencies, and in fact contain numerous unexplained modifications to the original data upon which the earlier study had relied.

46

Pacific's ability to operate under an X factor greater than the 5% currently in effect in California is confirmed by its election of 5.3% in the interstate jurisdiction.

50

The New Regulatory Framework as it presently exists has achieved its goals and, except for the increase in the X factor that is required to capture the effects of falling real input costs and growing productivity, the basic structure of the NRF should be retained.

53

### Appendix 1 Statement of Qualifications

Appendix 2 C. Anthony Bush and Mark Uretsky, "Input Prices and Total Factor Productivity," *First Report and Order*, FCC CC Docket 94-1, Released April 7, 1995, Appendix F.

Appendix 3 *An Empirical Estimate of the LEC Price Cap "X Factor" Based Upon Historic National LEC Productivity and Input Price Trends*, prepared by Economics and Technology, Inc. for the Ad Hoc Telecommunications Users Committee, and submitted with the Committee's *Reply Comments* in FCC CC Docket 94-1, June, 1994.

Appendix 4 Effect of Inconsistent Use of Short-run and Long-run Input Price Relationships in USTA/Christensen TFP study and X factor Development

## INTRODUCTION

**Qualifications**

Q. Please state your name, position and business address.

A. My name is Lee L. Selwyn. I am President of Economics and Technology, Inc., One Washington Mall, Boston, Massachusetts 02108. Economics and Technology, Inc. is a research and consulting firm specializing in telecommunications economics, regulation, management and public policy.

Q. Please summarize your educational background and previous experience in the field of telecommunications regulation and policy.

A. I have prepared a Statement of Qualifications, which is annexed hereto as Appendix I.

Q. Have you previously testified before the California Public Utilities Commission?

A. Yes, I have participated in numerous proceedings before this Commission dating back to the mid-1970s. These have included Pacific Telephone general rate case Applications 55492, 58223, 59849, 83-01-022 and 85-01-034. I have also testified in the Commission's generic Centrex rate and cost inquiry, Case 10191; in the Service Cost Commission's OII 83-02-01 investigation regarding policy development for intrastate exchange access charges and competition; at the Commission's *en banc* hearings on intra- and interLATA telecommunications policy in November, 1984; in the revenue requirements, rate design, and modernization and utilization phases of Application 85-01-034; in the GTE Mobilnet proceeding, A.83-07-04; in OII 87-11-031 dealing with the D.E.A.F. surcharge, in the Los Angeles area ZUM Expansion proceeding (A.87-01-002/I. 87-02-025), and in Application 90-11-011 involving so-called CLASS services.

1 I have also participated in all phases of the Commission's *New Regulatory Frameworks*  
2 investigation, I.87-11-033, beginning with written comments submitted in response to the  
3 Commission's August 11, 1987 Notice of *En Banc* Hearing on Competition and Regula-  
4 tory Reform. I participated in the settlement workshops in Phase I, and submitted  
5 testimony in Phase II, Phase III, the "Touch Tone/ELCA" phase, and in the Implemen-  
6 tation and Rate Design (IRD) phase. I also submitted testimony in the first triennial  
7 review of the New Regulatory Framework, A.92-05-002/004. In 1993, I appeared as a  
8 witness for the Commission's Division of Ratepayer Advocates (DRA) in the PacTel  
9 cellular/wireless "spin-off" investigation, I.93-02-028, and was an invited speaker at the  
10 Commission's *en banc* hearings on infrastructure issues in July, 1993.

11  
12 I have also participated in several previous proceedings involving the Pacific Bell  
13 Information Services Group (ISG) and PBIS issues — Application 88-08-031, the  
14 Company's proposal to offer an enhanced services "gateway," in Application 92-12-052,  
15 in which Pacific sought separate subsidiary status for ISG under the name "Pacific Bell  
16 Information Services," and Application 93-11-031 which was to authorize PBIS to enter  
17 the so-called "electronic publishing" business on a "below the line basis."

18  
19 **Assignment**

20  
21 Q. On whose behalf is this testimony being submitted?

22  
23 A. This testimony is submitted on behalf of California Committee of Large Telecommuni-  
24 cations Consumers (CCLTC).

25  
26 Q. What was the nature of your assignment in this proceeding?

27  
28 A. I have been asked to review the current scope and operation of the New Regulatory  
29 Framework (NRF) as modified by the Commission in D.94-06-011 and to develop and

- 1 offer specific recommendations to the Commission for modifications, if any, that may be
- 2 required to the NRF in light of the forthcoming onset of local exchange service
- 3 competition.



## 1 OVERALL EFFECTIVENESS OF THE NEW REGULATORY FRAMEWORK

2  
3 **There is no need or basis for any fundamental change in the structure of NRF at this**  
4 **time, although certain "mid-course corrections" should be considered.**  
5

6 Q. What criteria should the Commission use in assessing the various proposals for revision  
7 of the New Regulatory Framework that are being advanced in this investigation?  
8

9 A. The purpose of incentive regulation — and of the NRF in particular — is to de-link rates  
10 from costs and to shift risk (and reward) from ratepayers to management and share-  
11 holders, while at the same time providing a net benefit to ratepayers in the form of lower  
12 rates that capture the improved efficiency with which utilities subject to incentive  
13 regulation are expected to operate. As such, any changes to the NRF should be limited  
14 to *refinements* and to *mid-course corrections* of the system's parameters to reflect  
15 knowledge gained during the first five-plus years of operation, rather than to effect  
16 fundamental changes or reforms.  
17

18 In fact, the Commission did not anticipate making fundamental revisions to the NRF  
19 when it first adopted the incentive regulation system in 1989. At that time, the  
20 Commission held that the periodic reviews were "...an opportunity to evaluate the  
21 effectiveness of the chosen details and balance in the adopted regulatory framework, and  
22 to make any mid-course corrections that may be needed."<sup>1</sup>  
23

24 And that was certainly the position advanced by the LECs in the first triennial review of  
25 the NRF which began in May, 1992.<sup>2</sup> In a report prepared for Pacific Bell and

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26 1. D.89-10-031, 33 CPUC 2d 43 at 203.

27 2. A.92-05-002 (GTE-California); A.92-05-004 (Pacific Bell).